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DEPARTMENT OF STATE

ACTION MEMORANDUM

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Memo for the files: In view of recent agreement between Egypt & Libya I think this memo is not necessary. WM

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July 28, 1972

To: The Secretary

From: The Deputy Secretary

<u>Libya</u>

We are submitting the attached memorandum to the President without a recommendation. We would like your guidance on how you wish us to proceed.

Joe Sisco feels we should not make a recommendation to the President.

David Newsom, while recognizing that each of the three options presents risks, tends toward option two. He would recommend that we try clearly to separate the oil question from the arms question and talk to the companies about an approach to the Libyans which would emphasize the need to avoid abrupt and hostile action against the companies when they may be moving toward participation.

I tend to favor fulfilling our contract on the F-5 aircraft without seeking a specific <u>quid pro quo</u> on the oil company matter. This would remove an obvious irritant in our relations with Libya and might clear the way for less hostile discussions of our overall relations in the future. The rationale of proposing to begin the delivery of the aircraft could be the changed situation in the area, as well as our desire to improve relations with Libya.

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THE SECRETARY OF STATE
WASHINGTON

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MEMORANDUM FOR THE PRESIDENT

Subject: US-Libyan Relations

We have several indications suggesting that Libya may be seriously contemplating the partial (51%) or complete nationalization of one or more of the 13 U.S. companies which currently account for 90% of Libya's production.

Senior executives of the companies were summoned to Libya June 9 and were urged by Major Jallud, currently the Libyan Prime Minister, to urge the U.S. Government to change its policy in the Middle East and its policy on arms supply to Libya. A threat to move against the companies was implied.

Major al-Huni, another high ranking member of the regime, coupled the arms supply question with our Middle East policy in telling Ambassador Palmer on July 10 why he saw little prospect for cooperation between the United States and Libya.

Intelligence reports indicate that Libya may be preparing to nationalize some or all of the companies on or about September 1, the third anniversary of the military coup. Although such reports have been current in the past, these appear to have more substance to them. Libyan nationalization of the industry would be consistent with what we know of the aim of the Libyans to control their oil, the intense Libyan dissatisfaction with our policy in the Middle East and Colonel Qadhafi's desire to use oil as a political weapon against the United States.

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The Libyan regime also resents our refusal to supply it with certain fighter aircraft which were contracted for by the former government and for other military equipment (C-130's, howitzers, and possibly Sidewinders) which were not contracted for but which they have requested over the past two years. Particularly at issue are eight F-5 aircraft sold to the old regime in 1969 before the coup but not yet delivered and eight additional C-130's offered to them by Lockheed. We have been unwilling to give assurances that we would issue export licenses for these aircraft in 1973. The fact that we have continued to license spare parts for the F-5's and other military equipment we sold to them and that we have authorized the Italians to sell Libya armored personnel carriers, howitzers, recoilless rifles and ammunition which we control through production licenses has not lessened the Libyan Government's resentment against our restrictive arms policy.

Nationalization of the Libyan oil industry would be a severe blow to American interests. The industry represents a billion dollars (book value) of U.S. private investment, although some of it (Esso) has apparently already been largely written off. The industry returns as much as $400 million annually to our balance of payments. It produces about two million barrels of oil a day, chiefly for Western European markets, which would be irreplaceable. Loss of the oil, coupled with the shutdown of the Iraq Petroleum Company, would almost certainly force European consumers to come to terms with both Iraq and Libya, possibly bypassing the U.S. companies and discounting any U.S. official opposition. The position of those in the Arab world and elsewhere who wish to nationalize American assets would be strengthened. The move toward nationalization has already gained momentum in the Persian Gulf area and elsewhere in OPEC.

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Deputy Secretary Irwin has recently discussed the Libyan situation twice with oil company executives at the senior vice-presidential level, reviewing for them what we might do to head off nationalization. The executives expressed the hope that the U.S. might find some symbolic gesture it would make, at least to buy time.

We believe we have three options:

1. We could offer to deliver the eight F-5's for which we signed a contract in 1969 (in the trainer version now desired by Libya). As a symbolic gesture we might offer to deliver two planes by the end of the year and the rest within a year. The purpose of this action would be two-fold: to buy time during which perhaps the Libyans would not take any precipitate action against our companies, and to buy enough time for Saudi Arabia and the Gulf States to negotiate with the oil companies a reasonable settlement of the "participation" issue. We believe the chances of a reasonable settlement would be diminished if the Saudis and the other moderates were confronted by a total Libyan take-over of the American companies; in such circumstances they would find themselves under pressure to nationalize completely as well.

Even if the Libyans were to respond positively to our offer and we were to obtain a few months time, the basic problem would not be solved. There can be no guarantee that this or any other offer to Libya of a modest arms supply relationship will be effective, even in the short term. We believe Libya will move against the companies whenever it believes it can extract the maximum political and economic advantage. Arms deliveries will not permanently deflect Libya from such a move; at best, they may delay it. Such a delay should make a satisfactory settlement of the oil companies in Iraq more probable and should make the move toward total nationalization throughout OPEC less likely

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over the near to mid-term. One of the serious disadvantages of this option is that it would link arms supply and oil in the Libyan mind, thereby opening us to Libyan blackmail.

We must recognize nevertheless that the Libyans are attaching importance to obtaining some arms from us despite their extensive acquisitions from the French and the Russians. This is the only action they have hinted could lead to improved relations with the U.S. or at least to a less hostile attitude toward the oil companies. Under this option we would make clear to the Libyans that we expect improved relations would follow this gesture. If at any time during the period of the delivery of the aircraft Libya moved against the companies, shipments could be stopped and so could shipments of spare parts for the aircraft and other equipment of American origin that Libya now has in its inventory. Although Libya could assume that its ploy of linking arms and oil had worked and could ask for more sophisticated equipment (such as Sidewinders and C-130's), each new case could be discussed for a long period and deliveries prolonged over an extended period of several years. Libyan oil will decline in relative importance during the next decade, and any additional time the companies might have to operate in Libya would be valuable.

Although Israel could be mollified by an advance warning of our action and an explanation of it, any supply of arms to Libya would present grave problems both domestically and with more moderate countries in the Mediterranean area. Libya has intervened in the internal affairs of Morocco, has supported extreme Palestine groups, and has supported dissidents in numerous countries.

2. <u>We could support orderly nationalization</u>. The greatest threat in Libya is that of an abrupt and hostile nationalization which would cut off oil supplies and jeopardize the payment of compensation to the companies.

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Under this option, subject to consultation with the companies, we would indicate to the Libyans that we recognize their desire for increased participation and that we will not oppose participation along lines agreed upon between Saudi Arabia and Aramco. At the same time we would urge the Libyans not to undertake any sudden or preemptive nationalizations since this would obviously create difficulties for the kind of smooth transition which is in the interest of all parties. We would emphasize that we continue to believe that future production rests on arrangements between the companies and Libya in which the U.S. Government and its official policies are not involved.

Saudi Arabia and Aramco are currently negotiating a partial nationalization which would begin with a 20% participation by the government in Aramco increasing to 51% probably over a period of five years. At least two of the American Aramco partners and probably a third are resigned to accepting such an arrangement with the most serious bar to agreement probably residing in the terms for compensation. The settlement reached in Saudi Arabia is to apply also to Libya in accordance with the OPEC arrangements. Most of the American companies in Libya are prepared to accept this fact, but their willingness to do so has not been communicated by them to the Libyans who may, in any event, want more than 51% and want it sooner than five years.

If the U.S. were to accept the option of orderly nationalization and indicate its acceptance to the Libyans, it would be taking a step less palatable to the oil companies than a "symbolic" political or military gesture. Also, it could put the U.S. in the position of appearing to support nationalizations. The option could not be exercised without further high level consultations with the companies.

The main advantage of this option would be its separation of the oil and arms supply issues from each other. Having

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received from us an indication that we accepted the principle of nationalization, Libya would know that it could not use the threat of nationalization to force military supply or political concessions.

3. Take no action. On the assumption that the Libyans will proceed to nationalize on their own timetable and that any intervention on our part is not likely to be effective, we could take no action.

While there are signs of a clear Libyan intention to move at some point against some or all of the companies, we have no firm evidence that they have made such a decision. We have no certainty that the interventions proposed under options 1 or 2 would achieve the purpose of buying time or detering nationalization. We have made clear to the Libyan Government and to the companies our current policy of not supplying arms to Libya. Although the companies would like to have us make a symbolic gesture, they understand the difficulties we face in doing so. The Libyans probably do not expect further moves from us.

Under these circumstances we could continue to talk with the Libyans along the lines of our present policy but take no action specifically with respect either to the planes or to the question of nationalization.

The disadvantages of this are that it leaves us open to charges that we have not been sufficiently active in protecting the major American interests involved. The advantage would be that it would not draw us further into the efforts by Libya to use the companies to extract arms and changes in policy from us.

We are submitting the foregoing for your review and for such guidance as you desire to give the Department in this matter.

William P. Rogers

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